UNITED CONSUMERS
CREDIT UNION

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Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

Dear Members of the Board,

I appreciate the opportunity to comment on NCUA's proposed rule governing corporate credit unions and hope that the enclosed comments will be taken into serious consideration. While I do not believe the entire regulation is bad and needs to be scrapped, I do think it has some serious flaws.

After reading this regulation, listening to several corporate credit union staff members around the nation and attending three town hall meetings I have concerns as to whether these changes are in the best interest of our industry. In fact, if I were to rename this regulation, I'd call it the **"Let's get rid of Corporate Credit Unions so that it can never happen again"** regulation. Below, I've listed some of my general concerns regarding the regulation:

- NCUA doesn't appear to have had any outside investment expert model their ALM assumptions until after the regulation was written, according to comments made at the Dallas Town hall meeting. Due to the complexities of the corporates' investment portfolios, and considering that NCUA is not in the investing business, it would have seemed prudent to have done this before issuing such an all encompassing regulation.

- Maybe she is actively involved behind the scenes, but GiGi Hyland, who has a wealth of experience and background with corporate credit unions, seems to be nowhere in sight. Her expertise and insight regarding the corporates is too valuable to relegate her to the back of the room as at the Orlando Town hall meeting.

- This regulation creates an uneven playing field for corporates who will have to compete against banks that do not have the same investing restrictions placed on them. As a result, corporates will be forced to make up the lost investment income by charging higher fees than the banks, who subsidize their fees with other earnings. The corporate system was created to support credit unions because the banks were charging too much for needed services. This regulation seriously impairs the corporates' ability to remain competitive and could ultimately cause them to fail. If that happens, credit unions will once again be at the mercy of the banks.

- The supplementary information contained in the regulation shows that the investment portfolio can yield enough income to provide a healthy bottom line. Yet, I've heard from over 20 corporates around the nation who say they don't think they can survive with the restraints as they are under the new regulation. This is because of the restrictive investment and ALM rules and the unrealistic income assumptions used in the regulation's commentary.

- <u>The 1% retained earnings requirement needs to be eliminated</u>. This does not mean that corporates shouldn't be expected to earn a profit, but the amount of that profit should not be a regulatory requirement. The regulation restricts the corporates' ability to make money and imposes a demanding timeline to raise capital. It also requires corporates to earn a higher profit with fewer assets while offering fewer services. The elimination of the retained earning requirement will allow Corporates to raise the needed capital (PCC and NCA) and retain the affordable services that are valuable to credit unions.

- The NCUA stated at the town hall meeting in Dallas that there are too many corporates, but it's the large corporates who are in trouble. There is nothing in the events of last two years that would support the "economies of scale" argument that bigger is better. I would argue for more smaller corporates, as that way no single corporate is too big to fail.

- I believe that the NCUA knows how to audit a corporate credit union, but I'm not sure they really understand how a corporate operates day to day. There is huge difference between running the business and auditing one.

- We've heard over and over, "Never again!" in regards to the corporate crisis. Investing involves risk, if it didn't no one would pay any interest. You can't regulate the risk out of the business without destroying it. Managing risk is what financial institutions do. The regulation needs to allow corporates to manage that risk, not eliminate it.

- Some of the large natural person credit unions, who don't use or want corporates, are extremely involved in their redesign. Corporate credit unions provide the most value to the small and medium size credit unions that will have a much harder time surviving without them. NCUA should focus on who the end users are and what services they will need.

- NCUA staff and board members have stated, based on their observations, that credit unions are not willing to recapitalize their corporates. I believe this to be a faulty assumption and this is not what we've heard in Missouri. I believe credit unions are making these comments for three reasons:

  - Credit unions are unsure of what is involved in recapitalizing the corporates and will not commit until the rules are clear.
  - Under the proposed regulation, belonging to a corporate credit union will not provide enough benefits to offset the additional capital contribution required. Credit unions will:
    - Have to contribute more capital (NCA and PCC)
    - Have to pay substantially higher fees to offset the loss of income to meet the retained earnings requirement
    - See fewer services being provided.
    - Need to seek other investment options because of restrictions.
  - Credit unions are mad. When the dust settles credit unions will see the need to recapitalize the corporates if value remains.

  With this regulation NCUA is stripping out a lot of what is valuable in the relationship between a credit union and their corporate.

- The 90-day comment period is too short considering the length and depth of this proposed regulation. Credit unions still have their own shops to run and this is a complex issue.

Below I have attempted to outline my issues under each area of the regulation.

1. Capital

Overall, I don't have a huge problem with using the BASEL standards except for the arbitrary retained earnings requirement. The issues I have are that:

- Banks do not have the same investment/ALM limitations that corporates will have under the proposed regulation. This makes the corporates less competitive in two areas. First, earnings from the investment portfolio will be less due to the tighter investment restrictions so they may not be able to offer competitive rates. Second because of the reduced income and the new retained earning requirement, corporates will have to significantly increase their fees compared to banks who will still be able to subsidize these fees. It will be difficult to convince the credit unions to recapitalize the corporates when they realize it will cost them more for less service.

- The regulation is defining how estimated losses are handled differently from what is required by GAAP. This is being done only to validate NCUA's earlier interpretation and has no accounting basis. It is my understanding that FASB is likely to change the credit impairment model standards in 2010 to allow OTTI reversals as loss projections improve. NCUA should not be taking a different position in establishing their standards from that taken by the FASB.

- <u>The 1% retained earnings requirement needs to be eliminated to allow the corporates the ability meet the BASEL capital objective and still remain competitive</u>. There is no accounting basis for requiring an arbitrary 1% retained earnings ratio. This capital could be raised as perpetual contributed capital (PCC) that would allow the corporates more time to build their retained earnings while still providing value to their member credit unions.

  I'm not stating that a corporate should not be profitable, but it just doesn't make sense to put this type of requirement into the regulation if the corporate can raise sufficient capital from their membership.

  Implementing the retained earnings requirements creates a double penalty for the credit unions by making them contribute capital and then charging them substantially more to use the corporate.

2. Investments

- I agree with establishing concentration limits by investment sector, but would caution that they not be so restrictive as to prevent an acceptable return. As I stated earlier in this letter, if you remove all the risk from the portfolio, you also remove all the earnings.

- In my discussions with corporates, the example used by NCUA in the proposal regarding the sample investment portfolio is unrealistic and most believe the stated earnings could not be achieved. Most corporates I spoke with predicted an ROA much lower (around 0 to 7 basis points) than the 34 bp predicted in the proposal. This projected income is much less than the 15bp required in the proposed regulation.

- Investments under the regulation take a back seat to other services provided by the corporates (payment systems and providing liquidity). It would be difficult for corporates to produce enough income from those products alone to remain competitive. Corporates need to have viable investment options so they can continue to provide the products and services needed by credit unions.

3. Asset Liability Management

- The regulation does not take into account core deposits which will decrease the corporates' ability to mismatch funds for investment purposes. In most ALM scenarios, core deposits continue to exist and only in an extreme situation are those funds in jeopardy. It is not responsible to write a regulation based on the worst-case scenario. Again, the risk needs to be managed, not eliminated.

- The establishment of a two-year average life on the investment portfolio could seriously impair the corporates' ability to achieve sufficient yield to remain competitive. As proposed by other credit unions, I would suggest a three year weighted average life and that Agency and government-guaranteed securities be treated separately with a longer weighted average life restriction of five years.

- As the regulation stands now, corporates will have difficulty providing overnight investments to natural person credit unions. As a result natural person credit unions will have to manage this on their own. While this is not an issue for the larger credit unions, it will be a huge issue for those smaller credit unions who may not have investment expertise on staff.

4. Corporate Governance

- The proposed rule creates six-year term limits for corporate board members. I like the idea of term limits but suggest that nine years better serves the needs of both NCUA and the corporate. In NCUA's support of shorter-term limits you note in the commentary to the regulation that "Corporate management requires a high level of sophistication and expertise" yet that level of expertise takes time to develop. While a new Board member may ask more questions an experienced Board member will be able to use the knowledge they have gained to make a more informed decision.

In conclusion, I believe that NCUA has good intentions, but I worry about the "never again" mentality I have heard over and over again. Be careful not to swing the pendulum so far the other way that the corporates cannot survive. The decisions you make regarding this regulation will not only affect the corporates, but all of us. **Let the rule of reason prevail and not one of panic.**

Thank you for this opportunity to express my views concerning this regulation.

Sincerely,

Chris McCreary

Chris McCreary
President
United Consumers Credit Union